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Supreme Court of the United States

OCTOBER TERM, 1945.

No. .

PAUL H. SMART,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI.

*To the Honorable the Chief Justice of the United States
and the Associate Justices of the Supreme Court of
the United States:*

The above named petitioner prays that a Writ of Certiorari be issued to the United States Circuit Court of Appeals for the Second Circuit to review a judgment of that Court (R. 86) rendered in the above case on December 6, 1945, confirming a decision of the Tax Court of the United States which had sustained a determination of the Commissioner of Internal Revenue of a deficiency of petitioner's income tax for the calendar year 1941 (R. 24). A timely petition for rehearing was denied on December 21, 1946 (R. 93).

Jurisdiction.

The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended (28 U. S. C. A. Sec. 347 (a)).

The Opinions of the Court Below.

The opinion of the Tax Court (R. 9-23) is officially reported in 4 T. C. 846. The opinion of the Circuit Court of Appeals for the Second Circuit (R. 81-85) is reported in 152 Fed. 2nd 333.

Statute and Regulations Involved.

The statute involved is Section 107 of the Internal Revenue Code as amended by Section 139 of the Revenue Act of 1942. The relevant portion reads as follows:

Revenue Act of 1942.

SEC. 139. COMPENSATION FOR SERVICES RENDERED FOR A PERIOD OF THIRTY-SIX MONTHS OR MORE.

(a) Section 107 is amended to read as follows:

"SEC. 107. COMPENSATION FOR SERVICES RENDERED FOR A PERIOD OF THIRTY-SIX MONTHS OR MORE.

"(a). Personal Services:—If at least 80 percentum of the total compensation for personal services covering a period of thirty-six calendar months or more (from the beginning to the completion of such services) is received or accrued in one taxable year by an individual or a partnership, the tax attributable to any part thereof which is included in the gross income of any individual shall not be greater than the aggregate of the taxes attributable to such part had it been included in the gross income of such individual ratably over that part of the period which precedes the date of such receipt or accrual."

(b) The amendment made by subsection (a) shall be applicable to taxable years beginning after December 31,

1940, but with respect to a taxable year beginning after December 31, 1940, and not beginning after December 31, 1941, the period specified in such subsection shall be sixty months in lieu of thirty-six months, and the percentage specified in such subsection shall be 75 per centum in lieu of 80 per centum.

The regulations involved are Reg. 111, Sec. 29.107-1.

Summary Statement of Matter Involved.

The petitioner was a testamentary trustee who qualified and acted under the laws of the State of New Jersey. During the period from 1933 to 1940 he received, at intervals, and paid an income tax in each year of receipt, commissions for collecting income computed at the statutory rate of 5%. In 1941 he received, pursuant to a decree of the Prerogative Court of the State of New Jersey, the sum of \$73,197.93 as corpus commissions for actual services rendered in administering the principal of the trust from May 21, 1933 to October 7, 1940. No previous payment for, or on account of, administering the principal had been received by, or paid to, petitioner.

The petitioner contends that the New Jersey Court found certain identifiable services to have been rendered by petitioner for administering the corpus of the trust and that the sum of \$73,197.93 was allowed as compensation therefor; that such sum constituted "total compensation for personal services" rendered by him in administration of the corpus of the trust over a period of more than sixty (60) months and that he is therefore entitled to the benefits of Section 107 of the Code as amended by Section 139 of the Revenue Act of 1942.

The Court below denied this contention and held that the aggregate of both income and corpus commissions

constitute the "total compensation for personal services"; that therefore the lump sum corpus commissions received in 1941 was less than seventy-five percent (75%) of the total compensation and the petitioner did not come within the benefits of the taxing statute.

Question Presented.

Did the Circuit Court of Appeals err in holding that corpus commissions paid to a New Jersey testamentary trustee in 1941 for services rendered from May 21, 1933 to October 7, 1940, did not constitute total compensation for personal services within the meaning of Section 107 of the Internal Revenue Code as amended by Section 139 of the Revenue Act of 1942?

Facts.

The facts are undisputed.

The petitioner, a New York attorney, and Josiah Macy Willets, were designated as trustees, and the Fidelity Union Trust Co. as substituted trustee, under the will of Walter G. Ladd, who died May 21, 1933. The will was probated in the Prerogative Court of the State of New Jersey on June 1, 1933 (R. 47).

The trust comprised two substantial pieces of non-income producing real property requiring an annual maintenance charge of approximately \$130,000.00, and securities and personal property valued at approximately \$10,000,000.00 (R. 27 to 29, 57).

From the inception of the trust in 1933 through the tax year 1941, the petitioner received the statutory commission of 5% on all income collected which he included

in his tax returns for the year of their respective receipts. The aggregate of such income commissions was \$68,260.90 (R. 48-49).

On October 7, 1940, the co-trustee Willets died. In November, 1941, the petitioner and the representative of the deceased trustee filed an account in the Prerogative Court of the State of New Jersey and made application, for the first time, for compensation for administering the principal of the trust from the inception thereof to the date of the death of the co-trustee (R. 48).

The application was opposed in the Prerogative Court by the life tenant and the substituted trustee, but after a hearing before the Court the objections were overruled and by decree of the Court, the petitioner and the representative of the deceased trustee were allowed the sum of \$146,395.97 which was divided equally between the petitioner and the estate of the deceased trustee (R. 64).

The petitioner apportioned, in his income tax return for the calendar year 1941, the \$73,197.93 so received over the years 1934 through 1939 in accordance with the provision of Section 107 of the Internal Revenue Code as amended by Section 139 of the Revenue Act of 1943 (R. 48-49).

The Commissioner disallowed the apportionment and determined a deficiency of \$19,043.68, and the Tax Court sustained the respondent's determination (R. 24).

The Circuit Court sustained the determination of the Tax Court.

The Decisions Below.

The Tax Court considered that its decision in *Civiletti v. Commissioner*, 3 T. C. 1274, involving a New York testamentary trustee was controlling and held that in deter-

mining the petitioner's "total compensation for personal services" there must be added to his commissions for administering the principal, the commissions received by him for collecting income; and that for the purpose of applying Section 107 of the Code as amended the determination of the Court of the State of New Jersey was immaterial (R. 22) and that the petitioner received less than seventy-five percent (75%) of the total compensation in 1941 and as a consequence did not come within the benefits of the taxing statute.

The determination of the Tax Court was affirmed by the Circuit Court of Appeals. It said that "one underlying purpose of Section 107 was to relieve fiduciaries of the high surtaxes which they cannot avoid since Courts will not entertain repeated accountings"; that the case turned on whether the services for which principal commissions were awarded were separable from those for which the income commissions were awarded and concluded that "although the question is not free of doubt in the absence of some authoritative ruling to the contrary, we think that unless the State Court bases its award of commissions upon income and principal upon a corresponding separation of services, in applying Section 107 both payments should be brought into a hotchpot and the prescribed percentage computed accordingly".

Reasons Relied On for Allowance of This Writ.

The Writ of Certiorari should be issued because the Court below was in error and its decision conflicts in principle with the applicable decisions of this Court holding that the determination of the valid rules of local law should be left to the local courts and holding that the Federal Courts in applying the revenue laws must give

effect to the local law (*Blair v. Comm.*, 300 U. S. 5; *Helvering v. Stuart*, 317 U. S. 154).

The Writ of Certiorari should also be issued for the reason that a substantial question of Federal law is involved which affects a large number of taxpayers and is of importance in the administration of the revenue law.

Civiletti v. Comm., 152 Fed. 2nd, 332, was decided contemporaneously with the instant case by the same Court and a petition for a Writ of Certiorari is now pending in this Court. In that case the Court below was confronted with a New York testamentary trustee whose principal commissions were received in 1940 and consequently were governed by Section 107 of the Internal Revenue Code as originally enacted. The nature of the service performed and the problem of the percentage of income commissions to principal commissions were the same as in the case at bar.

In *Civiletti v. Comm., supra*, the Court below ignored entirely the payment on account factor represented by the income commissions which was the basis for its decision in the instant case and rested its decision squarely upon the ground that Civiletti had failed to complete his services at the time he received his compensation. Despite its own decision in the instant case, the Court indicated that if the question had arisen under the amendment involved herein a different result would have followed for the requirement of completion had been eliminated by the amendment.

The two decisions cannot be reconciled and will create uncertainty and confusion in determining the proper application of the taxing statute in the case of trustees receiving corpus or principal commissions. An important

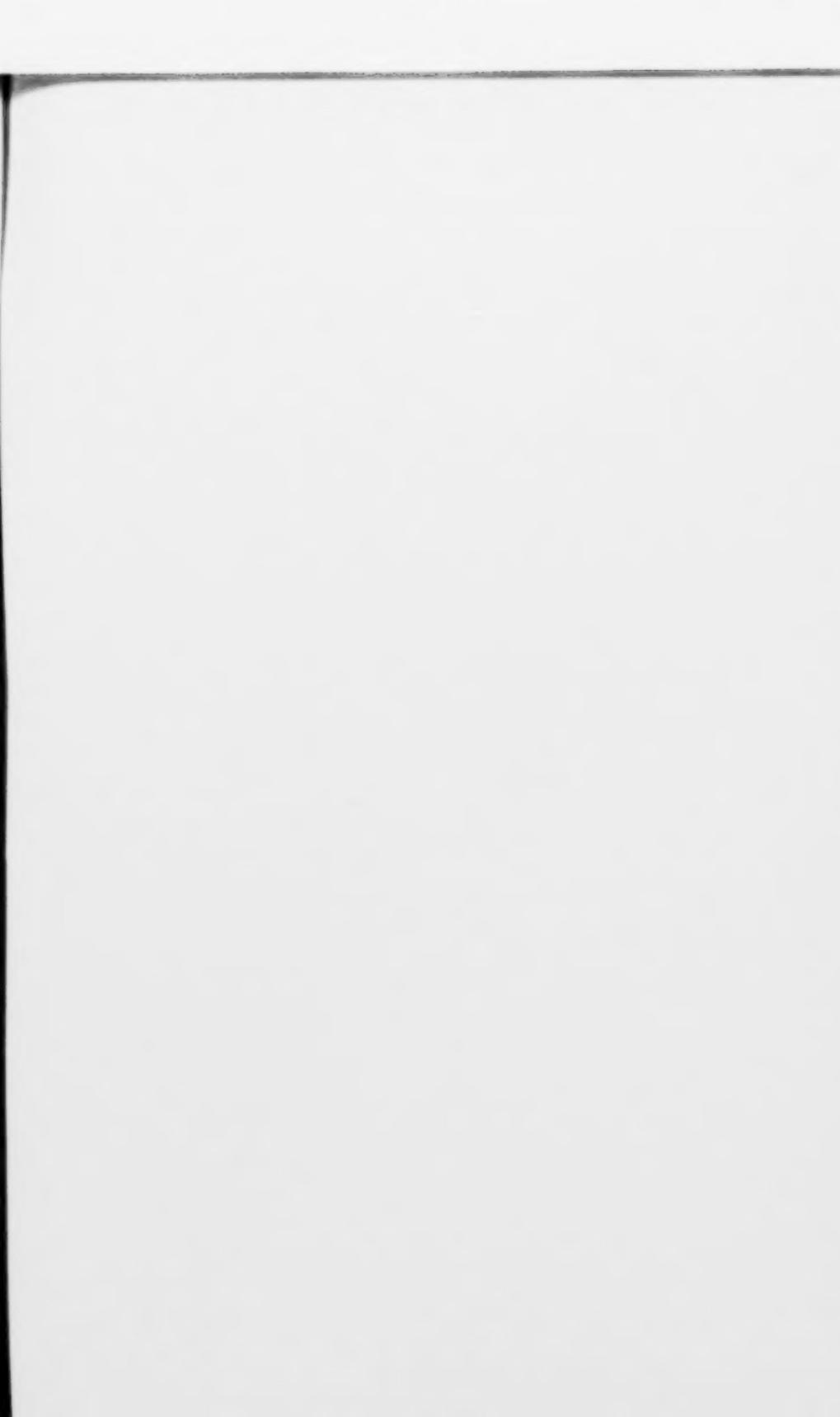
question of federal law is involved herein which has not been, and should be, decided by this Court.

WHEREFORE, your petitioner respectfully prays that a Writ of Certiorari issue under the Seal of this Court to review the decision of the Circuit Court of Appeals for the Second Circuit in the above case.

Dated, New York City, March 5, 1946.

PAUL H. SMART, Petitioner,

By: JULIUS L. NEIDLE,
Counsel for Petitioner.





Supreme Court of the United States
OCTOBER TERM, 1945.

No.

PAUL H. SMART,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

Question Presented, Statement of Case, Statutes, etc.

The statement of the question presented, the statement of the case, and the statutes involved will be found in the petition.

Specifications of Errors and Summary of Argument.

I. The Circuit Court of Appeals erred in holding that corpus commissions paid to a New Jersey testamentary trustee in 1941 for services rendered from May 21, 1933 to October 7, 1940, did not constitute total compensation for personal services within the meaning of Section 107 of the Internal Revenue Code as amended by Section 139 of the Revenue Act of 1942. Such decision is directly contrary in principle to the decisions of the Supreme

Court involving the recognition to be accorded the local law in applying a revenue measure.

II. An important and substantial question of Federal law is involved which has not been, and should be, settled by the Supreme Court.

POINT I.

The Circuit Court of Appeals erred in holding that corpus commissions paid to a New Jersey testamentary trustee in 1941 for services rendered from May 21, 1933 to October 7, 1940, did not constitute total compensation for personal services within the meaning of Section 107 of the Internal Revenue Code as amended by Section 139 of the Revenue Act of 1942. Such decision is directly contrary in principle to the decisions of the Supreme Court involving the recognition to be accorded the local law in applying a revenue measure.

In 1941 the petitioner, as co-trustee, received \$73,197.93 as his one-half ($\frac{1}{2}$) share of corpus commissions for services rendered from 1933 through 1940.

The allowance was made upon the application of the petitioner in the course of an intermediate accounting before the Prerogative Court of the State of New Jersey. Proof of the services was submitted to the Court in affidavit form (R. 50-61). The application was contested by the life tenant and the substituted trustee (R. 63). After hearing and deliberation by the Court the objections were over-ruled and the allowance was made and incorporated in the Decree in the following language:

"It is further ordered that there be allowed to Paul Smart and Gladys B. Willets, administratrix of the

estate of Josiah Macy Willets, deceased trustee the sum of One Hundred Forty Six Thousand Three Hundred Ninety Five and 87/100 Dollars (\$146,395.87) as commissions on corpus *for services rendered* by Paul Smart and Josiah Macy Willets, from May 21, 1933, the date on which said trust was set up, until October 7, 1940" (R. 64). (Italics ours.)

The same Decree approved and allowed income commissions to the trustees at the statutory rate of five percent (5%) on income collected (R. 65).

The New Jersey Revised Statutes, Title 3:11-1 and 3:11-2 the relevant portions of which are printed at page 19 of the appendix provide that a trustee shall receive five percent (5%) on all the income and "may take such income commissions as of the time when the income was or is received by them without allowance thereof by the Court".

With respect to the payment of corpus commissions the statute reads:

"3:11-1. Corpus Commissions in General. Allowance of corpus commissions to Executors, Administrators with the will annexed, Guardians and Trustees under a will, shall be made with reference to their actual pains, trouble and risk in settling the estate, rather than in respect to the *quantum* of the estate."

Section 2 of the same act provides:

"Where the corpus receipts exceed Fifty Thousand (\$50,000.00) the Court before which the account shall be presented for settlement and allowance shall determine the corpus commissions of Executors, * * *, and Trustees under a will, on the intermediate or final settlement of their accounts according to the *actual services rendered*. * * *." (Italics ours.)

The State of New Jersey has outlined a comprehensive scheme for compensation to trustees. It recognizes that two types of services are rendered, one in connection with collection of income and the other in connection with the administration of corpus. It provides a definite measure of compensation for each type of services; for services to income, five percent (5%) of the income collected when it comes into the hands of the trustees without Court order; for services to corpus, the value of the actual services rendered, to be determined by the Court before whom the application is made and to be paid only upon direction of the Court.

The taxing statute is clear and unambiguous and was enacted to relieve taxpayers who work for extended periods of time and receive their compensation in a lump sum (Rept. of the Senate Finance Comm. No. 648, 76th Congress, 1st Sess.). It states, with respect to the tax year 1941, that if a taxpayer receives at least seventy-five percent (75%) of the total compensation for personal services rendered covering a period of sixty (60) calendar months or more he may allocate the payment so received over the period in which the work was performed and compute his tax at the rates prevailing over that period.

The Tax Court recognized that two types of services were rendered by the petitioner (R. 20) but in applying the taxing statute to the case of a testamentary trustee held in effect that "personal services" meant personal services both for administering principal as well as collecting income and that "total compensation" meant the total of all compensation for both types of services. The Tax Court further held that it was immaterial upon what basis the corpus commissions were allowed by the State Court (R. 22). In an earlier case, *Additon v. Comm.*, 3 T. C. 427, the Tax Court had held that the "services" re-

ferred to in Section 107 signified those services for which the compensation in question were paid.

The Court below did not accept the reasoning of the Tax Court and said that the case turned on whether the services for which the corpus commissions were awarded were separable from those for which the income commissions were awarded, and concluded that "although the question is not free of doubt in the absence of some authoritative ruling to the contrary, we think that unless the State Court bases its award of commissions upon income and principal upon a corresponding separation of services, in applying Section 107 both payments should be brought into a hotchpot and the prescribed percentage computed accordingly."

The Court below makes no reference in its opinion to the controlling New Jersey statute. It brushes aside the entire judicial proceeding in the Prerogative Court of the State of New Jersey which included a hearing in open Court, the taking of proof of the services rendered, the application for an allowance for these services, the objection to the allowance and the Decree of the Court, and in the place of the actual proceedings held and the Decree therein rendered, the Court below has substituted its own interpretation of the judicial process of the State Court in the following language:

"When a court comes to award commissions to a trustee for his services, it does indeed divide the burden, because the services have inured to the benefit of both the life tenant and the remainderman, who for that reason ought to share the cost. But in so doing the court does not even impliedly try to separate the services into those which have benefited the income and those which have benefited the principal; on the contrary it divides the cost, either by some

rule of thumb, statutory or judge-made, or according to the supposed benefit, or in some other of the ways which courts are accustomed to measure the incom-mensurable."

The decision of the Court below disregards the legislative intent of the State of New Jersey fixing separate standards of compensation to trustees for two types of services and seems to render meaningless the judicial process of the New Jersey court which took proof of the services performed and awarded "commissions on corpus for services rendered by Paul Smart * * * from May 21, 1933 * * * until October 7, 1940" (R. 64). That this compensation relates only to services to corpus is evident from the fact that separate compensation for collecting income for different periods of time is allowed in a further portion of the Decree (R. 65).

The local court did indeed divide the burden of compensation between the life tenant and remainderman but it also determined the separate value of the separate services to corpus in accordance with the settled rule that corpus commissions are measured directly by the value of the services rendered to corpus. *Babbitt v. Fidelity Trust Co.*, 72 N. J. E. 745; *In re Account of New Jersey Title Guarantee and Trust Company*, 76 N. J. E. 293.

In the *Babbitt* case, *supra*, the Court said with respect to corpus commissions at page 761:

"* * * where a trustee has a very large estate, such as this one was, of a most varied character, handed over to it, and is required by the rule, applied to it by the Court, to exercise due diligence in the calling in of all unauthorized investments, and the duty of investing in authorized securities, it should be paid

a proper sum to compensate it for this labor and the responsibility and risk involved."

In *New Jersey Title Guarantee and Trust Company, supra*, the trustee served for seven (7) years but no corpus commissions were allowed for failure to establish any demonstrable service rendered to corpus.

We respectfully submit that the decision below should be reviewed by this Court and a Writ of Certiorari should be issued because the decision of the Court below is in error and conflicts with the rule laid down by the Supreme Court that the interpretation of the local laws should be left to the local courts and that a taxing statute of the Federal Government must give effect to the local laws and the decree of the local court (*Blair v. Comm.*, 300 U. S. 5; *Helvering v. Stuart*, 317 U. S. 154).

POINT II.

An important and substantial question of Federal law is involved which has not been, and should be, settled by the Supreme Court.

The question presented affects every testamentary trustee in the State of New Jersey as well as testamentary trustees in the several states of the union. It raises an important question in the orderly administration of the revenue law for the Court below has expressed doubt and uncertainty as to the proper application of the law, in the absence of an authoritative ruling. The question has been passed upon only in the case at bar and in *Civiletti v. Comm.*, 3 T. C. 1274, affirmed 152 Fed. 2nd 332. In view of the uncertain state of the law, prolific litigation will ensue before the Tax Court and in the various circuits to determine the proper application of the

taxing statute to the compensation received by testamentary trustees.

In the *Civiletti* case the taxpayer was a testamentary trustee acting under the laws of the State of New York. He received a lump sum principal commission payment in 1940 and contended that he was entitled to the benefits of Section 107 of the Internal Revenue Code as originally enacted.

The amendment involved herein differs from the original act in that it changes the prescribed period over which the work is to be performed, reduces the permissive percentage that may be paid on account and eliminates the requirements contained in the original act that the compensation shall be received on completion of "such services".

The Tax Court in the *Civiletti* case held that the "total compensation for services rendered" within the meaning of the taxing statute included both principal and income commissions and that the income commissions heretofore received by the taxpayer were payments on account which exceeded the permissive percentage. The Tax Court considered it unnecessary to determine whether the services were completed.

The Tax Court considered that the decision in the *Civiletti* case was controlling upon the instant case.

Inasmuch as payments of corpus or principal commissions are episodic and necessarily cover work performed over an extended period of time and income commissions are paid to or retained by trustees without an accounting upon income collected at regular intervals, the fiduciary, under the reasoning of the Tax Court, except in isolated cases, can not avail himself of the benefits of the taxing statute because the aggregate of the income commissions, if considered payments on account, would exceed the per-

missive percentage. The reasoning of the Tax Court would seem contrary to the rule of this Court that a taxing statute should be construed to effect equality among all taxpayers of a class (*Colgate-Palm-Olive-Peet Co. v. U. S.*, 320 U. S. 422, 425, 429). There is no distinction between an individual fiduciary and any other person who renders personal services (*Clark v. Comm.*, 3 T. C. 676).

The Circuit Court of Appeals in reviewing the decision of the Tax Court in the *Civiletti* case did not refer to or apparently consider the payment of income commissions as a factor in the case. It denied relief to the petitioner on the ground that the services had not been completed at the time the compensation was received which it said was a necessary requirement under Section 107 as originally enacted. It seems to hold that in a case coming under the present amendment a New York testamentary trustee could avail himself of the benefits of the statute and said "it would indeed be reasonable to allow the exemption to any taxpayer who receives in one sum the payment for five (5) or more years' services and that is just what Congress did when it amended Section 107 by Section 139 of the Revenue Act of 1942".

In the instant case which involved the amendment the Court below denied the exemption to the petitioner although it would seem that under the language quoted above the Court should have held to the contrary. In view of the remedial purpose declared by the Court below to underly the statute and in view of its own doubt, the Court below was in error for the Supreme Court has said that a tax law "is to be construed liberally in favor of the taxpayers to give the relief it was intended to provide" (*Bonwit Teller & Co. v. U. S.*, 283 U. S. 258, 263) and that "if the words are doubtful that doubt must be resolved against the government and in favor of the tax-

payer" (*U. S. v. Merriam*, 263 U. S. 179, 188). *Slough et al. v. Comm.*, 147 Fed. (2nd) 836 (C. C. A., 6th Cir.).

The *Civiletti* case and the instant case involve testamentary trustees who performed substantially identical services and who received principal or corpus commissions after an extended period of time during which they received income commissions in excess of the permissive percentage. In the instant case the Court below considered receipt of income commissions as a payment on account of total compensation and therefore dispositive of the issue presented; in the *Civiletti* case the Court did not consider the income commissions at all. It would seem difficult, if not impossible, to reconcile the two decisions and develop a rational basis to serve as a guide for the proper application of the taxing statute to the case of trustees.

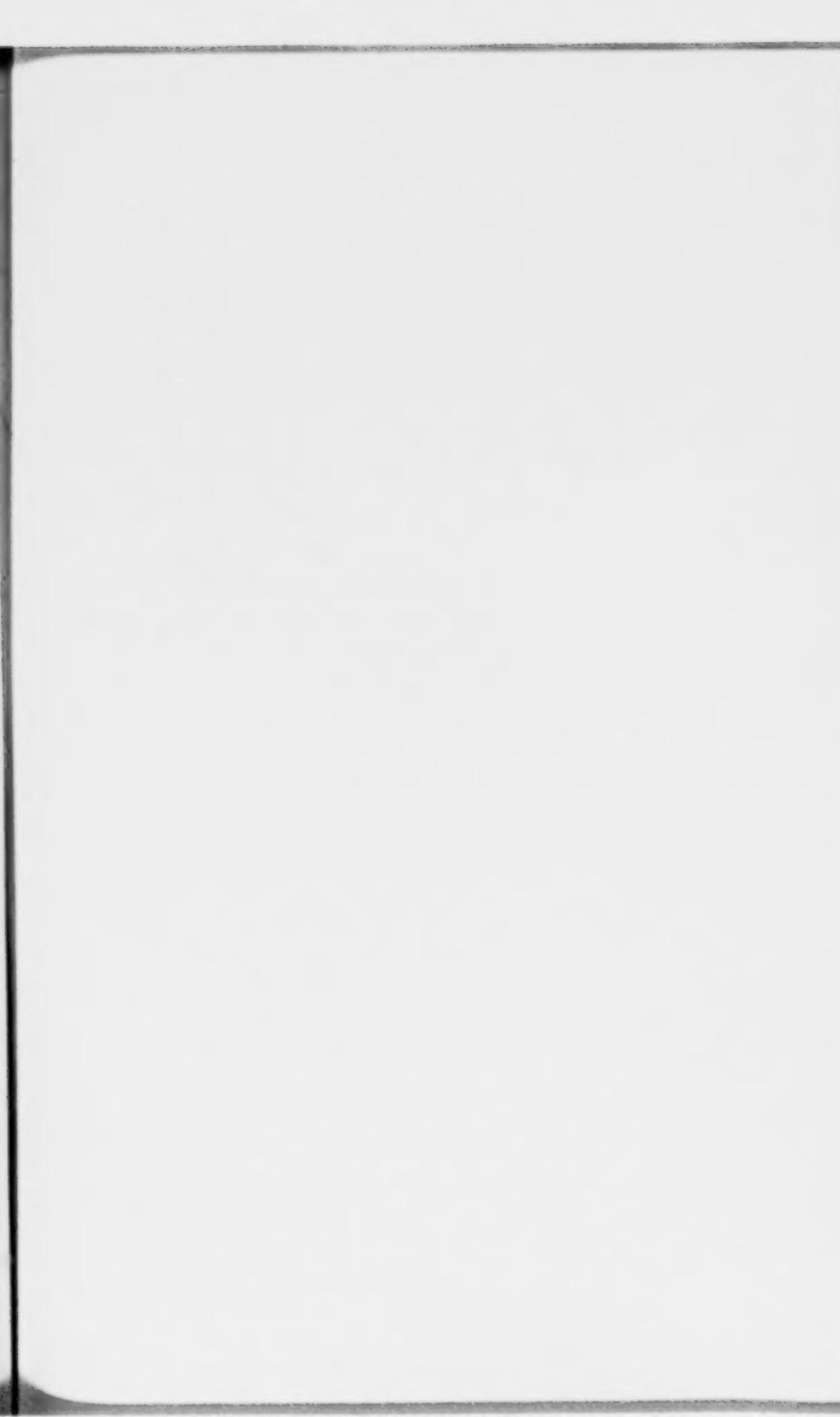
We respectfully submit that the decision below should be reviewed by this Court and a Writ of Certiorari should be issued because the question involved affects all testamentary trustees qualified and acting under the laws of the several states and is of importance in the orderly administration of the Internal Revenue laws and should be authoritatively settled by this Court. *Helvering v. National Grocery Co.*, 304 U. S. 282; *Interstate Transit Lines v. Comm. of Int. Rev.*, 319 U. S. 590; *Riggs v. Del Drago*, 317 U. S. 95.

CONCLUSION.

For the foregoing reasons it is respectfully submitted that the Petition for Writ of Certiorari to the Circuit Court of Appeals for the Second Circuit should be granted.

Respectfully submitted,

JULIUS L. NEIDLE,
Counsel for Petitioner.





APPENDIX.**New Jersey Revised Statutes, Title 3:11-1.**

Corpus Commissions in General. Allowance of corpus commissions to executors, administrators with the will annexed, guardians and trustees under a will, shall be made with reference to their actual pains, trouble and risk in settling the estate, rather than in respect to the quantum of the estate.

New Jersey Revised Statutes, Title 3:11-2.**Computation of commissions; rates**

On the settlement of accounts of executors, administrators, administrators with the will annexed, guardians and trustees under a will, accounting in the Prerogative or Orphans' Court, their commissions over and above their actual expenses shall be computed upon the following rates:

On all income that comes into their hands five per centum (5%) and such executors, administrators, administrators with the will annexed, guardians, and trustees under a will, may take such income commissions as of the time or when the income was or is received by them without allowance thereof by the court.

Where the corpus receipts exceed Fifty thousand dollars (\$50,000.00) the court before which the account shall be presented for settlement and allowance shall determine the corpus commissions of executors, administrators, administrators with the will annexed, guardians, and trustees under a will, on the intermediate or final settlement of their accounts according to the actual services rendered, and the commissions on corpus, shall not exceed five per centum (5%) on all corpus which comes into their hands; provided, however, that corpus commissions may be allowed in excess of the rates herein fixed in any case where the administration of the fiduciary has extended or extends beyond a period of twenty-five years.

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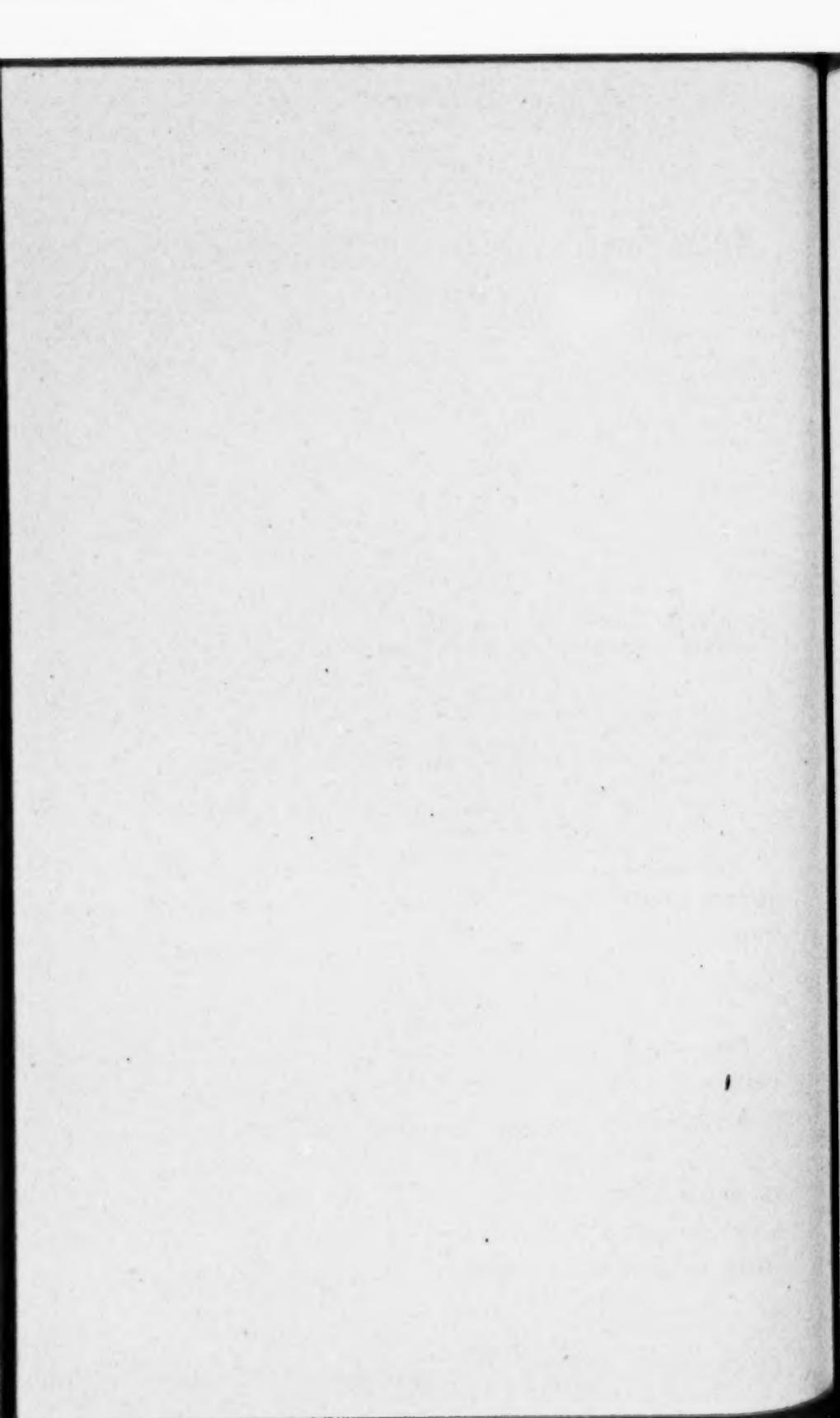
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In the Supreme Court of the United States

OCTOBER TERM, 1945

No. 912

PAUL H. SMART, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED
STATES CIRCUIT COURT OF APPEALS FOR THE SECOND
CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Tax Court (R. 18-23) is reported in 4 T. C. 846. The opinion of the Circuit Court of Appeals (R. 81-85) is reported in 152 F. 2d 333.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on December 6, 1945. (R. 86-87.) Rehearing was denied on December 21, 1945. (R. 93.) Petition for a writ of certiorari was filed March 5, 1946. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the "principal" commissions awarded to a New Jersey testamentary trustee in 1941 are taxable under the special provisions of Section 107 of the Internal Revenue Code as amended by Section 139 of the Revenue Act of 1942.

STATUTES INVOLVED

The pertinent statutes are printed in the Appendix, *infra*, pp. 10-12.

STATEMENT

The relevant facts as stipulated (R. 47-49) and as found by the Tax Court (R. 11-18) are as follows:

The taxpayer, a New York attorney, and Josiah Macy Willets were named as trustees of the residuary trust under the will of Walter G. Ladd, who died on May 21, 1933, and whose will was probated in the Prerogative Court of the State of New Jersey on June 1, 1933. They acted jointly from May 21, 1933, to the date of the death of Willets on October 7, 1940. (R. 11, 47.)

The trust comprised two substantial pieces of real property, one in Short Hills, New Jersey, and one at Bar Harbor, Maine, and personal property valued at approximately \$10,000,000. (R. 11.)

The decedent directed the trustees to maintain the real property during the lifetime of his widow in the same manner in which it had been maintained by him and to pay the income from his

personal property to her. Upon the death of the widow, the trustees were directed to transfer the entire estate, both real and personal, less five charitable legacies, to a charitable corporation for the purpose of maintaining the real property as a home for deserving gentlewomen who were without funds and who needed rest, hospitalization and similar charitable attention. Income in excess of the requirements for maintaining the home was to be used in aiding persons recuperating from the effects of illness or impaired health. The balance of income, if any, was to be distributed to and among hospitals, medical schools and other educational institutions. The ultimate beneficiaries of the principal, both real and personal, were two hospitals and three schools. (R.11-12.)

Prior to December 28, 1937, the taxpayer and his co-trustee filed a "First Intermediate Account" in the New Jersey Prerogative Court, after which the court issued a decree ordering, among other things, that (R. 13)—

said accountants be allowed and paid out of the aforesaid balance of income the sum of \$58,836.64, as and for their commissions, being at the rate of 5% on \$1,176,732.75 income collected * * *.

After Willets' death and during November, 1941, taxpayer as surviving trustee and Fidelity Union Trust Company, as substituted trustee, filed a "Second Intermediate Account." In this account, in addition to an application for com-

missions on income at the rate of five per cent, an application was also made by taxpayer and the representative of the deceased trustee for the allowance of one and one-half per cent commissions on the corpus of the trust for the services rendered by taxpayer and Willets from May 21, 1933, to October 7, 1940. (R. 13-14.) On December 9, 1941, the court issued a decree which is in part as follows (R. 14-15) :

It is further ORDERED that there be allowed to Paul Smart and Gladys B. Willets, administratrix of the estate of Josiah Macy Willets, deceased trustee, the sum of * * * (\$146,395.87) as commissions on corpus for services rendered by Paul Smart and Josiah Macy Willets from May 21, 1933, the date on which said trust was set up until October 7, 1940, said allowance to be paid by Paul Smart and Fidelity Union Trust Company out of the foregoing balance of principal;

It is further ORDERED that there be allowed to Paul Smart and Gladys B. Willets, administratrix of the estate of Josiah Macy Willets, deceased, the sum of * * * (\$65,595.53) as and for commissions at the rate of 5% on \$1,311,910.60 of income collected by the said Paul Smart and Josiah Macy Willets, during the period from October 31, 1937 to October 15, 1940, of which sum \$24,958.08 was paid to Paul Smart and \$24,958.08 was paid to Josiah Macy Willets, on February 3, 1940, as shown in Schedule L of said account, and the balance of * * * (\$15,679.37) shall be paid to the said Paul

Smart and Gladys B. Willets, administratrix as aforesaid, by Paul Smart and Fidelity Union Trust Company out of the forgoing balance of income;

It is further ORDERED that there be allowed to Paul Smart and Fidelity Union Trust Company, trustees, the sum of * * * (\$12,089.62) as and for their commissions at the rate of 5% on \$241,792.45 of income collected by them during the period from October 15, 1940 until April 30, 1941, said allowance to be paid by the said Paul Smart and the Fidelity Union Trust Company out of the foregoing balance of income.

Pursuant to the two above-mentioned decrees, taxpayer received the following sums on the dates specified (R. 15):

December 28, 1937-----	\$29,418.32
February 8, 1940-----	24,958.08
December 29, 1941-----	87,082.43

In his tax return for the calendar year 1941 the taxpayer apportioned his commissions received on principal in that year (\$73,197.93 of the \$87,082.43) over the years 1934 through 1939, relying upon Section 107 of the Internal Revenue Code, as amended by Section 139 of the Revenue Act of 1942. (R. 16-17.)

The Commissioner determined that the taxpayer was not entitled to the relief provided by Section 107 (R. 18) and his determination was sustained by the Tax Court (R. 18-23) which concluded that taxpayer's principal commissions must be added to prior income commissions in computing "total

compensation for personal services"; as a result taxpayer was determined to have received less than 75 percent of that compensation in 1941 as the statute required. The Circuit Court of Appeals, being unable to find any indication in New Jersey law that income and principal commissions were awarded upon the basis of a distinct separation of services, affirmed the Tax Court. (R. 81-85.)

ARGUMENT

The decision of the Circuit Court of Appeals in this case is correct. That court did not fail to accord proper respect to state law, and no substantial question of importance is here presented.

Section 107 of the Internal Revenue Code (Appendix, *infra*) may be availed of only if 75 percent of "the total compensation for personal services" is received in the taxable year. In computing the "total compensation" for taxpayer's services the Tax Court and the Circuit Court of Appeals correctly took into account the commissions awarded with respect to income as well as the commissions awarded with respect to principal. Taxpayer's services as trustee cannot, as a practical matter, be separated into services rendered to income and services rendered to principal. The services of a trustee at the same time protect and improve the principal and protect and increase the income. Even though commissions are divided into income and principal commissions, this division, as the Circuit Court of Appeals ex-

plained, is an administrative device by which the cost is allocated between the income beneficiary and remainderman "either by some rule of thumb, statutory or judge-made, or according to the supposed benefit, or in some other of the ways which courts are accustomed to measure the incommensurable." However, in making this division "the court does not even impliedly try to separate the services into those which have benefited the income and those which have benefited the principal * * *." (R. 83.)

Taxpayer argues that a division of the cost indicates that the services are also separated, and that under New Jersey law the services are actually separately evaluated and compensated. He points to the terms of the New Jersey court's award and to the New Jersey statute which provides for rates of commissions payable out of principal and income, Revised Statutes of New Jersey (Cum. Supp.), Sections 3:11-1 and 3:11-2 (Appendix, *infra*), which he contends were ignored by the court below. The Circuit Court of Appeals did not disregard New Jersey law; instead it carefully considered the applicable New Jersey decisions and interpreted them to mean that principal and income commissions are correlatives in New Jersey. It found no basis for an assumption that New Jersey courts award income and principal commissions based upon a corresponding separation of services. In spite of the separate rates pro-

vided for income and principal commissions, the New Jersey statute merely establishes "standards of compensation." *In re Fidelity Union Title & Mortg. Guaranty Co.*, 136 N. J. Eq. 294. The New Jersey courts, in awarding principal commissions, do not look solely to the value of the services to principal, but instead appear to weigh the total services against commissions already awarded from both income and principal. *Van Houten v. Van Houten*, 45 N. J. Eq. 796; *Marsh v. Marsh*, 82 N. J. Eq. 176; *In re Fidelity Union Title & Mortg. Guaranty Co.*, *supra*. The cases relied upon by petitioner (Br. 14-15) do not appear to be contra or to establish that a New Jersey trustee's services are strictly separated into services to income and services to principal and that they are separately compensated.

This case presents no question of substantial importance inasmuch as the decision, which is based upon an interpretation of New Jersey law, can have application only to New Jersey trustees. For this reason, even if the opinion of the Circuit Court of Appeals in *Civiletti v. Commissioner*, No. 913, also pending on petition for a writ of certiorari in this Court, may be read to mean that a New York trustee's services are separately evaluated and compensated, there is no contradiction in the court's rationale, for the *Civiletti* case involves New York statutes and New York law.

CONCLUSION

The decision is correct. The Circuit Court of Appeals considered and grounded its conclusion on the applicable law. No question of substantial importance is presented to require review by this Court.

Respectfully submitted,

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SEWALL KEY,
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Special Assistant to the Attorney General.

MARCH 1946.

APPENDIX

Revenue Act of 1942, c. 619, 56 Stat. 798:

SEC. 139. COMPENSATION FOR SERVICES RENDERED FOR A PERIOD OF THIRTY-SIX MONTHS OR MORE.

(a) Section 107 is amended to read as follows:

"SEC. 107. COMPENSATION FOR SERVICES RENDERED FOR A PERIOD OF THIRTY-SIX MONTHS OR MORE.

"(a) *Personal Services.*—If at least 80 per centum of the total compensation for personal services covering a period of thirty-six calendar months or more (from the beginning to the completion of such services) is received or accrued in one taxable year by an individual or a partnership, the tax attributable to any part thereof which is included in the gross income of any individual shall not be greater than the aggregate of the taxes attributable to such part had it been included in the gross income of such individual ratably over that part of the period which precedes the date of such receipt or accrual.

* * *

(b) The amendment made by subsection (a) shall be applicable to taxable years beginning after December 31, 1940, but with respect to a taxable year beginning after December 31, 1940, and not beginning after December 31, 1941, the period specified in such subsection shall be sixty months in

lieu of thirty-six months, and the percentage specified in such subsection shall be 75 per centum in lieu of 80 per centum. (26 U. S. C. 1940 ed., Supp. IV, Sec. 107.)

Revised Statutes of New Jersey (Cum. Supp.):

ARTICLE 1. IN GENERAL

3: 11-1. *Corpus commissions in general.*—Allowance of corpus commissions to executors, administrators, administrators with the will annexed, guardians and trustees under a will, shall be made with reference to their actual pains, trouble and risk in settling the estate, rather than in respect to the quantum of the estate.

ARTICLE 2. IN PREROGATIVE AND ORPHANS' COURT

3: 11-2. *Rates.*—On the settlement of accounts of executors, administrators, administrators with the will annexed, guardians, and trustees under a will, accounting in the prerogative or orphans' court, their commissions over and above their actual expenses shall be computed upon the following rates:

On all income that comes into their hands five per centum, and such executors, administrators, administrators with the will annexed, guardians, and trustees under a will may take such income commissions as of the time or when the income was or is received by them without allowance thereof by the court.

On corpus where the corpus receipts do not exceed fifty thousand dollars, seven per centum on the first one thousand dollars thereof, five per centum on the next nine thousand dollars thereof, four per centum on the next ten thousand dollars

thereof, and three per centum on the excess.

Where the corpus receipts exceed fifty thousand dollars, the court before which the account shall be presented for settlement and allowance shall determine the corpus commissions of executors, administrators, administrators with the will annexed, guardians, and trustees under a will, on the intermediate or final settlement of their accounts according to the actual services rendered, and the commissions on corpus, shall not exceed five per centum on all corpus which comes into their hands.

